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Proposed statement of position : Reporting on the costs of start-up activities;Reporting on the costs of start-up activities; Exposure draft (American Institute of Certified Public Accountants), 1997, Apr. 22

American Institute of Certified Public Accountants. Accounting Standards Executive Committee

EXPOSURE DRAFT

PROPOSED STATEMENT OF POSITION

REPORTING ON THE COSTS OF START-UP ACTIVITIES

April 22, 1997

Prepared by the Accounting Standards Executive Committee
American Institute of Certified Public Accountants

Comments should be received by July 22, 1997, and addressed to Daniel Noll, Technical Manager, Accounting Standards, File 4323, AICPA, 1211 Avenue of the Americas, New York, NY 10036-8775 or via the Internet to DNOLL@AICPA.ORG

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Any individual or organization may obtain one copy of this document without charge until the end of the comment period by writing to the AICPA Order Department, Harborside Financial Center, 201 Plaza Three, Jersey City, NJ 07311-3881 or by visiting the AICPA's internet website at aicpa.org.

AICPA

April 22, 1997

Accompanying this letter is an exposure draft of a proposed Statement of Position (SOP), *Reporting on the Costs of Start-Up Activities*. A summary of the proposed SOP is included in the forepart of that document.

The purpose of this exposure draft is to solicit comments from preparers, auditors, and users of financial statements and other interested parties.

The proposed SOP would apply to all entities that prepare financial statements in conformity with generally accepted accounting principles applicable to nongovernmental entities.

Areas Requiring Particular Attention by Respondents

Comments are specifically requested on the following issues addressed by this exposure draft:

(1) This proposed SOP broadly defines start-up activities and provides examples of costs that are and are not within the scope of this proposed SOP. Is the guidance sufficient to help entities determine what costs are included in the scope of this proposed SOP? If not, what additional guidance should be included?

(2) This proposed SOP requires that entities expense costs of start-up activities as they are incurred. This proposed SOP would amend the guidance related to start-up costs in SOP 81-1, *Accounting for Performance of Construction-Type and Certain Production-Type Contracts*; SOP 88-1, *Accounting for Developmental and Preoperating Costs, Purchases and Exchanges of Take-off and Landing Slots, and Airframe Modifications*; Audit and Accounting Guide, *Audits of Casinos*; Audit and Accounting Guide, *Construction Contractors*; Audit and Accounting Guide, *Audits of Federal Government Contractors*. Should the costs of start-up activities be expensed as incurred, or should they be capitalized and amortized over some period? If they should be capitalized and amortized, what probable future economic benefits do those assets represent? Over what period should those costs be amortized?

(3) This proposed SOP does not require disclosure of start-up costs in an entity's financial statements. Should the proposed SOP require any disclosures in the financial statements?

(4) Though the financial reporting of organization costs are not addressed in the proposed SOP, AcSEC has purposely defined those costs more narrowly than the definition in the Internal Revenue Code. As a result, the proposed definition may cause temporary tax differences related to organization costs. Should organization costs be included in the scope and subject to the provisions of the proposed SOP? If not, should AcSEC define those costs in this document? Do you agree with the proposed definition of organization costs in paragraph 9? Is the definition too broad or too restrictive? Why? If you do not agree with the proposed definition and you believe organization costs should be defined in this document, please provide a definition.

AcSEC welcomes comments or suggestions on any aspect of the exposure draft. When making comments, please include references to specific paragraph numbers, include reasons for any suggestions or comments, and provide alternative wording where appropriate.

Comments on the exposure draft should be sent to Daniel Noll, Technical Manager, Accounting Standards, File 4323, American Institute of Certified Public Accountants, 1211 Avenue of the Americas, New York, NY 10036-8775, in time to be received by July 22, 1997. Responses may also be sent by electronic mail over the Internet to DNOLL@AICPA.ORG.

Written comments on this exposure draft will become part of the public record of the AICPA and will be available for public inspection at the AICPA's offices for one year after July 22, 1997.

Sincerely,

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SUMMARY

This Statement of Position (SOP) provides guidance on the financial reporting of start-up costs. It requires costs of start-up activities to be expensed as incurred.

The SOP broadly defines start-up activities and provides examples to help entities determine what costs are and are not within the scope of this SOP.

This SOP applies to all nongovernmental entities and is effective for financial statements for fiscal years beginning after December 15, 1997. Earlier application is encouraged in fiscal years for which financial statements previously have not been issued.

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FOREWORD

The accounting guidance contained in this document has been cleared by the Financial Accounting Standards Board (FASB). The procedure for clearing accounting guidance in documents issued by the Accounting Standards Executive Committee (AcSEC) involves the FASB reviewing and discussing in public board meetings (1) a prospectus for a project to develop a document, (2) a proposed exposure draft that has been approved by at least ten of AcSEC's fifteen members, and (3) a proposed final document that has been approved by at least ten of AcSEC's fifteen members. The document is cleared if at least five of the seven FASB members do not object to AcSEC undertaking the project, issuing the proposed exposure draft or, after considering the input received by AcSEC as a result of the issuance of the exposure draft, issuing the final document.

The criteria applied by the FASB in their review of proposed projects and proposed documents include the following.

1. The proposal does not conflict with current or proposed accounting requirements, unless it is a limited circumstance, usually in specialized industry accounting, and the proposal adequately justifies the departure.

2. The proposal will result in an improvement in practice.

3. The AICPA demonstrates the need for the proposal.

4. The benefits of the proposal are expected to exceed the costs of applying it.

In many situations, prior to clearance, the FASB will propose suggestions, many of which are included in the documents.

REPORTING ON THE COSTS OF START-UP ACTIVITIES

INTRODUCTION AND BACKGROUND

1. The Accounting Standards Executive Committee (AcSEC) has on its agenda a series of projects on reporting the costs of activities, such as start-up, training, customer acquisition, and similar activities, that are undertaken to create future economic benefits.

2. The first phase of AcSEC's series of projects resulted in its issuance of Statement of Position (SOP) 93-7, *Reporting on Advertising Costs*. It was AcSEC's intention to use SOP 93-7 as a guide in developing guidance for reporting costs of other kinds of activities undertaken to create future economic benefits. This SOP on start-up costs is the next phase of AcSEC's series of projects.

3. A review of a number of public-company financial statement disclosures indicates that some entities capitalize start-up costs while others expense start-up costs as they are incurred. In addition, entities use diverse amortization periods. These diverse practices exist within and across industries. AcSEC believes this SOP will significantly reduce these diversities in financial reporting.

SCOPE

4. For purposes of this SOP, start-up activities are defined broadly as those one-time activities related to opening a new facility, introducing a new product or service, conducting business in a new territory, conducting business with a new class of customer[1] or beneficiary, initiating a new process in an existing facility, or commencing some new operation. This SOP provides guidance on accounting for the costs of start-up activities.

5. Start-up activities relate to the periods before an entity commences operations or production and after operations have begun, but before normal productive capacity[2] is reached. Therefore, costs of start-up activities include learning costs and operating losses incurred before a project reaches normal productive capacity.

6. In practice, various terms are used to refer to start-up costs, such as preopening costs, preoperating costs, and start-up costs. For purposes of this SOP, these costs are referred to as start-up costs.

As noted in subsequent paragraphs, accounting for certain costs incurred during the start-up period are not covered by this SOP. The SOP makes no inference on the accounting for costs outside the scope of this SOP. An entity should not infer that costs outside the scope of this SOP should be capitalized unless those costs qualify for capitalization under other generally accepted accounting principles.

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[1] This SOP does not address the financial reporting of costs incurred related to on-going customer acquisition, such as policy acquisition costs in FASB Statement No. 60, *Accounting and Reporting by Insurance Enterprises,* and loan origination costs in FASB Statement No. 91, *Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases.* The SOP addresses the more substantive one-time efforts to establish business with an entirely new class of customers (for example, a manufacturer who does all of its business with retailers attempts to sell merchandise directly to the public).

[2] Normal productive capacity is defined as the average level of operating activity that is sufficient to fill the demand for an entity's products or services over a period of time.

7. For purposes of this SOP, activities related to the routine, ongoing efforts to refine, enrich, or otherwise improve upon the qualities of an existing product, service, process, or facility are not start-up activities and are not within the scope of this SOP. In addition, activities related to a merger or acquisition and to on-going customer acquisition[3] are not start-up activities.

8. The following costs related to start-up activities are outside the scope of this SOP:

- Costs of acquiring or developing tangible assets. However, the cost of using tangible assets that are allocated to start-up activities (for example, depreciation of computers used for start-up activities) is within the scope of this SOP.

- Costs of acquiring intangible assets from third parties. However, the cost of using intangible assets that are allocated to start-up activities (for example, amortization of a purchased patent during the start-up period) is within the scope of this SOP.

- Costs that are eligible to be capitalized as part of inventory, long-lived assets, or some other internally developed intangible assets. (However, paragraphs 14, 17, and 18 amend the accounting for certain costs included in inventory by certain entities.)

- Costs that are within the scope of Financial Accounting Standards Board (FASB) Statement No. 2, *Accounting for Research and Development Costs*, and FASB Statement No. 71, *Accounting for the Effects of Certain Types of Regulation.*

- Costs of fund raising incurred by not-for-profit organizations.

- Costs of raising capital.

9. Organization costs are also outside the scope of this SOP. For purposes of this SOP, organization costs are defined as costs of preparing: (1) the entity charter; (2) the partnership agreement; (3) the bylaws; (4) the minutes of organizational meetings; and (5) the terms of original stock certificates.

10. Illustrations 1 through 5 in the Appendix provide examples of costs that are and are not within the scope of this SOP.

11. This SOP applies to all nongovernmental entities and it applies to start-up costs of development-stage entities as well as established operating entities.

12. This SOP amends the following AICPA SOPs and Audit and Accounting Guides that address start-up costs:

a. SOP 81-1, *Accounting for Performance of Construction-Type and Certain Production-Type Contracts*, paragraphs 75(a) and (d).
b. SOP 88-1, *Accounting for Developmental and Preoperating Costs, Purchases and Exchanges of Take-off and Landing Slots, and Airframe Modifications*, paragraphs 23 and 25.
c. Audit and Accounting Guide, *Audits of Casinos*, paragraph 2.06.
d. Audit and Accounting Guide, *Construction Contractors*, paragraphs 2.14(a) and (d).
e. Audit and Accounting Guide, *Audits of Federal Government Contractors*, paragraph 3.09.

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[3] See footnote 1.

CONCLUSIONS

Accounting for Start-Up Costs

13. Costs of start-up activities should be expensed as incurred.

Amendments to Other Guidance

14. This SOP amends SOP 81-1 by requiring start-up costs to be expensed as incurred rather than charged to existing contracts.
The following sentence is added to the end of paragraph 75(a):

> Those costs should be expensed as they are incurred if they are determined to be within the scope of (this SOP).

Paragraph 75(d) is amended as follows:

> Learning or start-up costs incurred in connection with existing contracts and in anticipation of follow-on or future contracts for the same goods or services should be expensed as incurred.

15. This SOP amends SOP 88-1 by requiring preoperating costs to be expensed as incurred rather than capitalized. Paragraph 23 is amended as follows:

> Preoperating costs related to the integration of new types of aircraft should be expensed as incurred.

In addition, paragraph 25 is deleted.

16. This SOP amends the Audit and Accounting Guide, *Audits of Casinos*, by requiring preopening costs to be expensed as incurred. Paragraph 2.06 is amended to include the following at the end of the first sentence:

> Preopening costs, however, should be charged to expense as incurred.

17. This SOP amends the Audit and Accounting Guide, *Construction Contractors*, by requiring start-up costs to be expensed as incurred rather than charged to existing contracts. The following sentence is added to the end of paragraph 2.14(a):

> Those costs should be expensed as they are incurred if they are determined to be within the scope of (this SOP).

Paragraph 2.14(d) is amended as follows:

> Learning or start-up costs incurred in connection with existing contracts and in anticipation of follow-on or future contracts for the same goods or services should be expensed as incurred.

18. Paragraph 3.09 of the Audit and Accounting Guide, *Audits of Federal Government Contractors*, refers to paragraph 75 of SOP 81-1 as the applicable guidance for accounting for precontract costs. This SOP amends paragraph 3.09 of the Guide as follows:

Precontract costs should be accounted for in conformity with paragraph 75 of SOP 81-1, as amended by paragraph 14 of this SOP.

EFFECTIVE DATE AND TRANSITION

19. This SOP is effective for financial statements for fiscal years beginning after December 15, 1997. Earlier application is encouraged. Restatement of previously issued financial statements is not permitted.

20. The initial application of this SOP should be reported as the cumulative effect of a change in accounting principle, as described in Accounting Principles Board (APB) Opinion No. 20, *Accounting Changes*. When adopting this SOP, entities are *not* required to report the pro forma effects of retroactive application.

21. Initial application of this SOP should be as of the beginning of the fiscal year in which the SOP is first adopted.

The provisions of this Statement need not be applied to immaterial items.

BASIS FOR CONCLUSIONS

Scope

22. AcSEC based its broad definition of start-up activities on the definition used in the 1973 FASB Discussion Memorandum (DM), *Accounting for Research and Development Costs*. That DM defines start-up costs as "those unusual one-time costs incurred in putting a new plant into operation, opening a new sales outlet, initiating a new process in an existing plant, or otherwise commencing some new operation."

23. AcSEC could not develop an all-inclusive definition of start-up activities and start-up costs. AcSEC believes the broad definition of start-up activities together with the examples provided in the Appendix help the reader understand the kinds of activities and costs that may be involved in a start-up situation.

24. AcSEC understands that entities may engage in start-up activities to generate revenue or increase efficiencies; AcSEC believes that it is unnecessary to distinguish between the objectives for undertaking start-up activities for purposes of this SOP.

25. AcSEC recognizes that entities use the terms start-up, preopening, and preoperating interchangeably and inconsistently in practice. AcSEC believes that it is unnecessary to define the terms individually for purposes of this SOP.

26. AcSEC also recognizes that some differentiate between preopening/preoperating costs and start-up costs as follows:

- Preopening/preoperating costs are incurred before the commencement of operations or production.

- Start-up costs are incurred after operations have begun, but before normal productive capacity is reached.

AcSEC believes that this distinction is not made consistently in practice. AcSEC also believes that the guidance in this SOP should be followed regardless of the terms used to describe the activities included in the scope.

27. AcSEC decided that it was not necessary to develop boundaries for when the start-up phase begins and ends. AcSEC believes that many of the costs previously capitalized by entities as start-up costs will be expensed as incurred as start-up costs or some other costs, such as general and administrative.

28. This SOP provides guidance on accounting for the costs of start-up activities undertaken to create future economic benefits. The costs of acquiring intangible assets are excluded from the scope of this SOP because those costs are addressed in other authoritative literature, such as APB Opinion 17, *Intangible Assets*. Likewise, the costs of acquiring or developing tangible assets are addressed in other authoritative literature, such as chapter 9, "*Depreciation,*" in Accounting Research Bulletin (ARB) No. 43, *Restatement and Revision of Accounting Research Bulletins*.

29. AcSEC decided that costs incurred related to start-up activities that are eligible to be capitalized as part of inventory, long-lived assets, or internally developed intangible assets are excluded from the scope of this SOP. AcSEC did not attempt to provide an all-inclusive list of such costs because entities have different accounting policies for, say, the kinds of costs they capitalize as property, plant, and equipment. AcSEC believes entities are best capable of identifying those costs.

30. This SOP applies to start-up activities of development stage entities as well as established operating entities, as those terms are discussed in FASB Statement No. 7, *Accounting and Reporting by Development Stage Enterprises*. Paragraph 10 of FASB Statement No. 7 states, "Generally accepted accounting principles that apply to established operating enterprises shall govern the recognition of revenue by a development stage enterprise and shall determine whether a cost incurred by a development stage enterprise is to be charged to expense when incurred or is to be capitalized or deferred." This SOP sets forth the generally accepted accounting principles for costs of start-up activities and thus, applies to both kinds of entities.

31. Recognizing that organization costs are not defined in the broad authoritative financial accounting literature, AcSEC attempted to define those costs to help entities determine what costs are and are not covered by the SOP. AcSEC's definition of organization costs purposely limits the kinds of costs that would fall outside the scope of the SOP.

Accounting for Start-Up Costs

32. AcSEC considered requiring capitalization and amortization of the costs of start-up activities. AcSEC believes that entities incur costs related to start-up activities with an expectation that there will be future benefits. AcSEC believes that this is also often the case with other costs, such as costs related to research and development activities.

33. AcSEC believes that no evidence has been identified that demonstrates a direct causal relationship between start-up costs incurred and related future economic benefits; therefore, AcSEC reasons that those costs should be expensed as they are incurred. That reasoning is consistent with paragraph 49 of FASB Statement No. 2, *Accounting for Research and Development Costs*, which states ". . . evidence of a direct causal relationship between current research and development expenditures and subsequent future benefits generally has not been found." Paragraph 86 of FASB Concepts Statement No. 5, *Recognition and Measurement in Financial Statements of Business*

Enterprises, states, "Consumption of economic benefits during a period may be recognized either directly or by relating it to revenues recognized during the period . . . " Paragraph 148 of FASB Concepts Statement No. 6, *Elements of Financial Statements*, states, "Other costs are also recognized as expenses in the period in which they are incurred because the period to which they otherwise relate is indeterminable or not worth the effort to determine."

34. Paragraph 24 of APB Opinion 17 states, "costs of developing, maintaining, or restoring intangible assets which are not specifically identifiable, have indeterminate lives, or are inherent in a continuing business and related to an enterprise as a whole--such as goodwill--should be deducted from income when incurred." AcSEC believes entities are not able to identify the specific future period benefitted related to start-up costs incurred. Therefore, the future economic benefits resulting from costs of start-up activities have indeterminate lives and, if those costs were capitalized, amortization periods would be arbitrary.

Disclosure

35. AcSEC considered requiring entities to disclose start-up costs incurred in an accounting period and total start-up costs expected to be incurred over the life of a project. AcSEC decided that, for many entities, the costs of recordkeeping to separately identify start-up costs incurred in an accounting period likely would outweigh the related benefits of disclosing those costs to users of financial statements. In addition, AcSEC believes that, if an entity discloses total start-up costs expected to be incurred, it is likely to do so outside the financial statements (for example, in Management's Discussion and Analysis for a public company).

Other Authoritative Literature

36. AcSEC considered the following other authoritative literature in its deliberations of financial reporting of start-up costs. However, the guidance in the following literature is *NOT* affected by the provisions of this SOP: (a) FASB Statement No. 19, *Financial Accounting and Reporting by Oil and Gas Producing Companies*, and the related AICPA Audit and Accounting Guide, *Audits of Entities with Oil and Gas Producing Activities*; (b) FASB Statement No. 50, *Financial Reporting in the Record and Music industry*; (c) FASB Statement No. 51, *Financial Reporting by Cable Television Companies*; (d) FASB Statement No. 53, *Financial Reporting by Producers and Distributors of Motion Picture Films*; (e) FASB Statement No. 60, *Accounting and Reporting by Insurance Enterprises*; (f) FASB Statement No. 67, *Accounting for Costs and Initial Rental Operations of Real Estate Projects*; and (g) FASB Statement No. 91, *Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases*.

APPENDIX

The Illustrations provide examples that should not be interpreted to be all-inclusive. Accounting for certain costs incurred during the start-up period are not covered by this SOP. The SOP makes no inference on the accounting for costs outside the scope of this SOP. An entity should not infer that costs outside the scope of this SOP should be capitalized unless those costs qualify for capitalization under other generally accepted accounting principles.

ILLUSTRATION 1

Scenario - A major U.S. beverage company (the Company) acquires a majority stake in a local Chinese plant. This is the first beverage operation owned by the Company in China, and it represents the Company's initial entry into the Chinese market. As part of the overall strategy relative to the acquisition, the Company plans to introduce into China, on a locally produced basis, its major U.S. beverage brands. Following are some of the costs that might be incurred during the start-up period and how the Company should classify those costs:

<u>Start-up costs (that is, costs within scope of SOP)</u>

- Travel costs, employee salary-related costs and consulting costs related to feasibility studies, accounting, legal, tax, and governmental affairs.
- Training of local employees related to production, maintenance, computer systems, engineering, finance, and operations.
- Initial process and quality testing prior to operations.
- Recruiting, organization, and training related to establishing a distribution network.
- Operating losses incurred before normal production capacity is reached, and yield and volume variances.
- Depreciation, if any, of new computer data terminals and other communication devices during the start-up period.

<u>Costs outside scope of SOP</u> (as noted in paragraphs 7-9 of this SOP)

- Costs of capacity additions, such as production equipment and packaging lines.
- Costs of modernization efforts resulting in the betterment of existing equipment.
- Internal-use computer software systems development costs.
- Governmental fees, registration, and product approval costs.
- Production costs related to inventory.

ILLUSTRATION 2

Scenario - An entity manufactures medical equipment using a manual, labor-intensive process. The entity will incur $80 million in costs to implement a totally automated process that will enable the entity to manufacture entirely new medical equipment to perform laser surgery. The existing manual process does not provide the degree of precision needed to manufacture the laser equipment. The entity will initiate a new manufacturing process and reduce its workforce by 65 percent. It will also add 10,000 square feet to the existing facility. The new laser equipment is expected to increase annual sales by $60 million. Following are some of the costs that might be incurred during the start-up period and how the entity should classify those costs:

Start-up costs (that is, costs within scope of SOP)

- Consulting fees for outside consultants to help implement the new process. Consulting fees will include production flow improvement, employee training, and quality-assurance testing on initial production.

- Salary-related costs of eight management personnel who will devote 100 percent of their time to the changeover.

- Recruiting costs incurred to bring new highly skilled employees to the area. These costs include moving expenses, housing allowances, and bonuses.

- Utility, insurance, and security costs incurred before the plant begins production.

- Operating losses incurred before normal production capacity is reached, and yield and volume variances.

- Depreciation, if any, of new computer data terminals and other communication devices during the start-up period.

Costs outside scope of SOP (as noted in paragraphs 7-9 of this SOP)

- Consulting fees for outside consultants to help select manufacturing equipment and the computerized software operating system to run the equipment.

- Costs of manufacturing equipment and a computerized software operating system purchased from a third-party vendor.

- Debt issuance costs and interest on amounts borrowed to finance the plant addition.

- Architect fees on the plant addition.

- Severance and outplacement costs incurred in connection with the reduced workforce.

- Advertising costs to publicize the entity's entry into the laser-equipment market.

- Purchase of customer lists used to advertise the entity's new product.

ILLUSTRATION 3

Scenario - A restaurant chain is opening two new restaurants. One will open in a territory in which the entity already has three restaurants operating. The other will open in a new territory for the entity. (Regardless, costs related to both openings are treated the same for purposes of this SOP.) All of the restaurants provide the same products and services. Following are some of the costs that might be incurred during the start-up period and how the entity should classify those costs:

<u>Start-up costs (that is, costs within scope of SOP)</u>

- Salary-related expenses for new employees.
- Salary-related expenses for the management restaurant opening team.
- Training costs and meals for newly hired employees.
- Hotel charges, meals, and transportation for the opening team.
- Rent, security, property taxes, insurance, and utilities.
- Depreciation, if any, of new computer data terminals and other communication devices during the start-up period.
- Operating losses incurred during the start-up period.

<u>Costs outside scope of SOP</u> (as noted in paragraphs 7-9 of this SOP)

- Restaurant advertising costs.
- Coupon giveaways.
- Costs of silverware, dishes, salt and pepper shakers, glasses, coffee hottles, and pitchers.
- Costs of uniforms.
- Costs of tables, chairs, and cash registers.
- Costs to obtain liquor license.

ILLUSTRATION 4

Scenario - An entity is a manufacturer of rubber products. In the process of molding rubber into functional parts, there is an unavoidable by-product of excess rubber called "flash." The entity is initiating a new process and significantly modernizing its processes for removing (that is, deflashing) the excess rubber from manufactured functional parts. The entity will purchase new equipment and remove some of the old equipment. It will not increase the size of its manufacturing facility. Following are some of the costs that might be incurred during the start-up period and how the entity should classify those costs:

<u>Start-up costs (that is, costs within scope of SOP)</u>

- Costs of training existing employees to operate and maintain the new, state-of-the-art machinery.
- Employee salary-related costs for developing new policies and procedures for scheduling of production.
- Depreciation, if any, of new computer data terminals and other communication devices during the start-up period.
- Operating losses incurred before normal production capacity is reached, and yield and volume variances.

<u>Costs outside scope of SOP</u> (as noted in paragraphs 7-9 of this SOP)

- Purchase and installation of new deflashing equipment.
- Purchase of new computer data terminals and other communication devices for better scheduling and expediting.

ILLUSTRATION 5

Scenario - A not-for-profit organization that has provided meals to the homeless is opening a shelter to house the homeless. This will be the organization's first shelter and it will conduct a fund-raising campaign to raise money to start up the shelter. The organization will lease space for the shelter and will incur capital expenditures for leasehold improvements and furniture. The organization expects that it will require three months to set up the space for the shelter and an additional one month until it is operating at normal capacity. The organization will hire a security firm to secure the premises during the three-month period in which the shelter is built. Once the shelter is built, the security firm will remain on contract for the first four months that the shelter is open and operating. In addition, the shelter will hire five certified social workers for the first four months that the shelter is open and operating. Following are some of the costs that might be incurred during the start-up period and how the organization should classify those costs:

Start-up costs (that is, costs within scope of SOP)

- Employee salary-related costs related to needs and feasibility studies.
- Staff recruiting and training.
- Rent, security, insurance, and utilities during the start-up period.
- Consultant fees for developing policies and procedures for operating the shelter.
- Amortization and depreciation, if any, of leasehold improvements and furniture during the start-up period.
- Costs of the certified social workers until normal operating capacity is reached.

Costs outside scope of SOP (as noted in paragraphs 7-9 of this SOP)

- Costs of fund-raising
- Costs of leasehold improvements and furniture (other than amortization and depreciation, if any, during the start-up period)
- Government fees, registration fees, and inspection costs.
- Architect fees for the addition.
- Advertising costs to publicize the shelter.